Client Alert | US Public Company Advisory / Capital Markets

Key Considerations for the 2021 Annual Reporting and Proxy Season Part I: Form 10-K Considerations

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This is Part I of a two-part memorandum series outlining key considerations from White & Case's Public Company Advisory Group for US public companies during the 2021 annual reporting and proxy season.

Part I of this memo describes our key considerations for Annual Reports on Form 10-Ks in two parts:

(1) Housekeeping Items for Form 10-Ks in 2021; and

(2) Top Nine Disclosure Considerations for the Form 10-K in 2021.

Part II of the series will describe key considerations for Annual Meeting Proxy Statements.

Considerations for Annual Reports on Form 10-K in 2021

Recent SEC rulemaking and other developments in 2020 have resulted in a number of changes to SEC filings, including your upcoming 10-K, as described below.[1]

Housekeeping Items for Form 10-Ks in 2021

As a result of recent SEC rule changes, the following housekeeping items should be addressed for Form 10-Ks:

(1) Update 10-K Cover Page: First, make sure your Form 10-K cover page is updated to reflect the most recent change by ***adding*** the below language to the cover page.[2] All US public companies will need to check this new 10-K cover page box—unless they do not provide an attestation report by their independent auditors on internal control over financial reporting because of their status as an emerging growth company or a non-accelerated filer.[3]

> "Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the

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1 Including amendments to Regulation S-K Items 101, 103 and 105, which became effective November 9, 2020. For more information, see our prior alert "SEC Adopts Amendments to Modernize Disclosures and Adds Human Capital Resources as a Disclosure Topic: Key Action Items and Considerations for US Public Companies."

2 This change was adopted as part of the amendments to the accelerated filer and large accelerated filer definitions under Securities Exchange Act ("Exchange Act") Rule 12b-2, effective April 27, 2020, as further discussed below.

3 *See* Item 308(b) of Regulation S-K.

Sarbanes-Oxley Act (15 USC. 7262(b)) by the registered public accounting firm that prepared or issued its audit report. ☐"

This is the third year in a row in which changes have been made to the Form 10-K cover page.[4] Given all of these changes, it is important to confirm that your Form 10-K cover page reflects all recent updates.[5]

(2) Determine Your Filing Status: Second, confirm your filing status in order to complete your Form 10-K cover page. In particular, the SEC recently changed the definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 under the Exchange Act.[6]

- ☐ As a result of this change, an issuer is **not** an "accelerated filer" if the issuer (i) is eligible to be a smaller reporting company ("SRC") **and** (ii) had revenues of less than $100 million in the most recent fiscal year for which audited financial statements are available.
- ☐ However, an SRC with (i) a public float between $75 million and $250 million, and (ii) $100 million or more in annual revenues would still be an "accelerated filer" as well as an SRC in accordance with the June 2018 amendments to the definition of an SRC.[7]
- ☐ The determination of a company's filing status is crucial for determining the deadline for filing periodic reports for the fiscal year, among other requirements. *See* the SEC's compliance guide and information on filing deadlines.

(3) Check Exhibit Index: Companies should check their exhibit lists in light of recent changes to exhibit filing requirements in Item 601 of Regulation S-K. In particular, companies should ensure that they have reviewed and updated their exhibits in accordance with the 2019 changes to material exhibits as follows:

- ☐ ***Material Contracts No Longer Required If Fully Performed***: For companies that are not "newly reporting registrants,"[8] Item 601(b)(10) now requires material contracts to be filed only if they are to be performed in whole or in part ***at or after*** the filing of the report.[9] Accordingly, companies should review

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4 In 2018 and 2019 pursuant to additional rule amendments, the changes to the Form 10-K cover page consisted of the following:

- the ***addition*** of the trading symbols for all of your US-exchange-listed securities to the cover page in a table titled "Securities registered pursuant to Section 12(b) of the Act";
- the ***removal*** of the statement and checkbox regarding Section 16 delinquencies "Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K");
- the ***removal*** of language on "posting" the company's Interactive Data Files on its corporate website, so that the statement and checkbox reads "Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files)"; and
- the ***removal*** of language next to the non-accelerated filer checkbox that companies "not check" the box if they are a smaller reporting company.

For more information, see our prior alerts "Key Considerations for the 2020 Annual Reporting and Proxy Season" and "Reminders for US Public Companies for the 2019 Annual Reporting and Proxy Season."

5 The SEC website generally provides a current version of the SEC's forms, available here. Regulation S-K is available here.

6 The final rule is available here. In addition, the amendments adjust the transition thresholds to (i) $60 million when transitioning from an accelerated filer to a non-accelerated filer and (ii) $560 million when transitioning from a large accelerated filer to an accelerated filer.

7 The rule is available here.

8 The term as defined in Instruction 1 to paragraph (b)(10) of Item 601 includes companies that are not subject to Exchange Act reporting obligations and certain shell companies.

9 The previous rule had also required material contracts that were fully performed before the filing date but that were entered into within two years of the filing to be filed.

their exhibit index to check if any material contracts have been fully performed and can therefore be removed from the exhibit index as a result of this rule change.

- ***Schedules of New Exhibits***.
  - ***In General, May Omit Schedules from All Exhibits:*** Under paragraph (a)(5) of Item 601 of Regulation S-K, companies may now omit schedules and similar attachments to **all** exhibits, provided that: (i) the schedules/attachments do not contain material information; and (ii) the information in the schedules/attachments is not otherwise disclosed in the exhibit.
  - ***Provide List of Omitted Schedules, If Required:*** Amended Item 601(a)(5) requires companies that omit schedules to provide a list briefly identifying the contents of all omitted schedules, but this list is **not** required if the filed exhibit already includes this list or otherwise conveys the subject matter of the omitted schedules.
  - ***Remove Undertaking to Provide Omitted Schedules from Exhibit List.*** Under the SEC's prior rule on exhibit schedules, companies were only permitted to omit schedules from plans of acquisitions under Item 601(b)(2) if they filed a list briefly identifying the contents of all omitted schedules *together with* an agreement to furnish to the SEC a copy of the omitted schedules upon request. However, under the amended rule, this "agreement "is no longer specifically required and therefore disclosure regarding such an agreement (often provided in a footnote to the exhibit list) should be removed. Nevertheless, note that the new rule still states that, "upon request," a company "must provide a copy of any omitted schedule to the Commission or its staff."[10]
- ***Remove Personally Identifiable Information.*** In addition, Item 601(a)(6) of Regulation S-K explicitly allows a company to omit personally identifiable information from exhibits, such as bank account numbers, social security numbers, home addresses and similar information. Companies should take care to remove such personally identifiable information from their exhibits prior to their filing.
- ***Consider Recent Changes for Confidential Treatment Request Orders*:**
  - *Consider Confidential Treatment Requests for New Exhibits.* As a reminder, pursuant to amendments adopted in 2019, companies are permitted to omit confidential information from material contracts *without* having to submit a formal confidential treatment request ("CTR"), so long as the redacted information: (i) is not material; and (ii) would likely cause competitive harm to the company if publicly disclosed. Companies should follow the procedures for redactions described in recent Staff guidance, which also notes that the Staff is selectively reviewing filings for compliance.[11] As an alternative, companies can still use the traditional CTR process.[12]
  - *Check for Expiring Confidential Treatment Request Orders.* Prior to filing your 10-K, you should check if your company has any expiring confidential treatment orders on material agreements. Depending on the time period when the order was originally issued, there are different requirements to request a renewal of the order, as explained in SEC guidance issued in September 2020.[13]
- ***Consider, if Applicable, the New Registered Debt Exhibit***. Effective January 4, 2021, companies with registered debt securities that are guaranteed by related entities are required to file an Exhibit 22 under

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10 *See* the adopting release FN 192, available here.

11 For more information on the procedures for exhibit redactions, as well as information on Staff reviews of redacted exhibits, *see* Staff guidance, available here.

12 *See* Staff guidance updated in September 2020, available here. Also *see* prior Staff guidance on extensions available here.

13 *See* here.

new Regulation S-K Item 601(b)(22) listing (i) each affiliate whose securities are pledged as collateral for the company's debt securities; and (ii) the securities pledged.[14]

(4) Electronic Signatures

- ***Consider Using Electronic Signatures*.** Under prior SEC rules, all individuals were required to **manually sign** a signature page or other authentication document (the "authentication document") before or at the time of an SEC filing that provided their typed signature. Effective December 4, 2020, amended Rule 302(b) of Regulation S-T gives such individuals the option to sign the authentication document with an electronic signature, instead of with a manual, wet-ink signature.[15] Reporting companies will thus be able to file periodic and current reports and registration statements using authentication documents that have been signed electronically by appropriate parties, CEOs and CFOs will be able to electronically sign the authentication documents for certifications required to be filed with Forms 10-K and 10-Q, and filers of Schedules 13D/G and Section 16 reports (Forms 3, 4 and 5) will be able to do so as well. **However**, in order to use electronic signatures for authentication documents, companies must abide by the attestation requirement described below.
  - ***If Using an Electronic Signature, Remember the Attestation Requirement*.** Before a signatory initially uses an electronic signature to sign an authentication document for an SEC filing, the signatory must have manually signed a blanket attestation stating that the use of an electronic signature will, for all future SEC filings, constitute the legal equivalent of the individual's manual signature for authentication purposes. See **Appendix A** for a Sample Attestation**.** An electronic filer must retain this manually signed attestation for as long as the signatory may use an electronic signature to sign an SEC filing (and in any case, at least seven years after the date of the most recent electronically signed SEC filing) and furnish a copy of the manual signature to the SEC upon request.[16]
  - ***If Using Electronic Signatures, Establish Required Signing Process.*** In addition, companies using electronic signatures must abide by new processes established by the SEC. In particular, the signing process for electronic signatures is now set forth in the EDGAR Filing Manual[17] and requires a number of steps, including that the signatory "present a physical, logical or digital credential that authenticates the signatory's individual identity" and that the electronic signature "include a timestamp to record the date and time of the signature."[18]

Considerations for the Form 10-K in 2021

Below is our list of our top nine disclosure items to consider when preparing your upcoming Form 10-K in 2021.[19]

(1) Business Section: Add Human Capital Management Disclosure. Amended Item 101 of Regulation S-K requires, *to the extent such disclosure is material to an understanding of the company's business taken as a whole*, a description of human capital resources, including any human capital measures or objectives that the company focuses on in managing the business. The amended rule provides non-exclusive examples of such human capital measures and objectives (*i.e.*, "measures or objectives that address the attraction, development, and retention of personnel"), which may be material, depending on the nature of the company's business and workforce. However, each company's disclosure must be tailored to its unique business, workforce, and facts and circumstances. In additional, the amendments retain a

14 Under amendments to Regulation S-X Rules 3-10 and 3-16. *See* the adopting release, available here.

15 *See* the final rule amendment here and the press release here.

16 In addition, signatories who have provided others with SEC signing authority through powers of attorney ("POA") should execute an addendum to the POA granting such electronic signature authority.

17 *See* Section 5.1.2 of the EDGAR filing manual, available here.

18 *See* page 5 of the adopting release, available here.

19 For more information, *see* our prior alerts "SEC Adopts Amendments to Modernize Disclosures and Adds Human Capital Resources as a Disclosure Topic: Key Action Items and Considerations for US Public Companies" and "Practical Tips for Preparing Upcoming Quarterly Disclosures."

requirement from the prior rule to provide the total number of persons employed. In developing a company's human capital disclosure for its 10-K, companies should:

- ***Assess Existing Human Capital Disclosure.*** Consider the company's current, existing disclosure relating to human capital—including in risk factors of the 10-K and sustainability reports—in order to assess which information is available, verifiable and can be prepared without undue cost.
- ***Consider Board and Management Focus for Human Capital.*** Consider which human capital measures or objectives the board and senior management focus on in managing the business.[20]
- ***Consider Ramifications for Human Capital Disclosure.*** Consider the company's goals in providing this disclosure in its 10-K and understand the potential internal and external ramifications related to making such disclosure, including expectations of investors on a going forward basis.

In any event, legal departments should be reviewing drafts of human capital disclosure for liability risks and other issues, such as broad statements that may raise liability concerns due to lack of back-up support or controls processes. Although we expect many companies to take a moderate approach for this first year and weigh additional disclosures for subsequent years, the recent COVID-19 human capital disclosures in quarterly reports have provided many companies with a first step in the type of human capital disclosure that may be appropriate for this first year.[21]

Moreover, this new section of the Form 10-K is providing companies with an opportunity to provide more traditional ESG disclosure typically found in sustainability reports for the first time in 10-Ks, and to the extent this information is verifiable and does not give rise to undue litigation risk, it may be appropriate and even beneficial for a company to include for this year. Each company's facts and circumstances should be assessed for the appropriate level and type of disclosure for this new section.

(2) Revise Your Risk Factor Format.

- ☐ ***If Risk Factor Section is Over 15 Pages, Add Summary Risk Factor Disclosure:*** If a company's risk factor section exceeds 15 pages, the amended SEC rules, effective November 9, 2020, require the company to ***add*** a "series of concise, bulleted or numbered statements that is no more than two pages summarizing the principal factors that make an investment in the registrant or offering speculative or risky" and place this summary in the "forepart" or at the beginning of the Form 10-K. Many companies have chosen to combine this disclosure with their forward-looking statement legends in order to avoid repetition, and companies may consider this approach so long as the legend is titled to reflect its dual purposes (*i.e.*, "Cautionary Note Regarding Forward-Looking Statements and Risk Factor Summary"), and the Company confirms that the legend will now include the company's principal risk factors as well as those factors that could cause actual results to differ materially from the forward looking statements included in the filing (which in many cases may overlap, but should be reviewed carefully in light of **both** SEC requirements).
- ☐ ***Tailor Generic Risks or Add a General Risk Factor Section.*** For this year's 10-K, companies need to review their risk factor section to determine if it includes risk factors that apply generically to any

20 For more information on what human capital measures companies were disclosing in their Form 10-Ks prior to the effectiveness of the rule change, *see* our prior alert "ESG Disclosure Trends in SEC Filings."

21 For more information, *see* our prior alert, "ESG Disclosure Trends in SEC Filings." With respect to COVID-19-related disclosures, employee welfare, health and safety and business continuity issues took the spotlight in first quarter quarterly reports filed with the SEC. For example, in first quarter 10-Q filings, 38 out of 50 top companies by revenue in the Fortune 100 (or 76 percent) included disclosure on employee health and safety. Nearly all of these disclosures referenced COVID-19 and measures companies were taking to protect and promote employee welfare. Many companies also highlighted their business continuity planning in disclosures in light of potential COVID-related disruptions. SEC disclosure guidance in Topics No. 9 and 9A emphasized the importance of disclosing material information regarding employee matters due to the pandemic, such as employees' transition to remote working arrangements, the modification of operations to comply with health and safety guidelines to protect employees, and constraints on human capital resources and productivity. The impact of COVID-19 on corporate operations cannot be overstated, and investors are interested in how companies are responding in terms of safety, logistics, and operational continuity.

registrant or offering, and then either (i) tailor these risk factors to emphasize the specific relationship of the risk to your company, or (ii) disclose the generic risk factors at the end of the risk factor section under the caption "General Risk Factors".

- ***Organize Risk Factors Under Relevant Headings***: For this year's 10-K, companies will need to organize risk factors into groups of related risk factors under "relevant headings", in addition to the subcaption currently required for each risk factor. This is typically done in registration statements, and to the extent not provided in your 10-K, will need to be done before filing this year's 10-K.

(3) Assess your Business Section and Legal Proceedings Section in Light of SEC Rule Amendments Effective November 9, 2020.[22] In addition to the human capital disclosure described above, companies should consider the following for their business and legal proceedings sections:

- ***Required Discussion of Material Changes to a Previously Disclosed Business Strategy*.** Companies are now specifically required under Item 101(c) to disclose "material changes to a registrant's *previously disclosed* business strategy." This is particularly relevant for a company that recently went public and provided a lengthy discussion of its business strategy in the business section of its IPO registration statement. Companies should also consider previous disclosure in quarterly reports, earnings conference calls and other investor communications regarding business strategy, and assess whether there are any material changes to this disclosure, particularly in light of changes due to the recent COVID-19 pandemic. The SEC's adopting release emphasized the principles-based approach of the amendments and the ability of companies to determine the appropriate level of detail for these disclosures.

- ***Consider Streamlining Disclosure that May No Longer be Required.*** In its rule amendments for the Business section, the SEC emphasized its principles based approach and that information that is material to a company's business must be disclosed. At the same time, information that that was eliminated under the amendments to Item 101 of Regulation S-K and is not otherwise material for a company may be removed. For example, to the extent **not material** for a company, it may remove from its Form 10-K Business section: "the year in which the registrant was organized and its form of organization" and "the dollar amount of backlog orders". However, companies must provide disclosure on Business section topics (even those eliminated from Item 101(c)'s previous prescriptive disclosure list, as detailed in this chart in our prior memo) if material to an understanding of the business.[23]

- ***Confirm Your Business Section Includes a Discussion of Compliance with Material Government (Not Just Environmental) Regulations.*** Codifying common practice among reporting companies, amended Item 101(c) now specifically requires, to the extent material to an understanding of the business taken as a whole, disclosure of the material effects on capital expenditures, earnings and competitive position of compliance with **government regulations generally**, including but not limited to environmental regulations. Companies are also required to include the estimated capital expenditures for environmental control facilities for the current fiscal year and any other subsequent period that is material. Companies should ensure that regulatory disclosure in their Form 10-Ks adequately addresses all areas of government regulations generally that are responsive to this principles-based materiality standard.

- ***Assess Your Environmental Legal Proceedings Disclosure.*** In reviewing their environmental legal proceedings disclosure, companies should consider recent amendments to the requirements for environmental legal proceedings under Item 103 of Regulation S-K, which add two points of flexibility to existing disclosure requirements.

  - ***Modified $300,000 Threshold for Environmental Proceedings Disclosure.*** Amended Item 103, which requires companies to disclose any proceeding under environmental laws to which a governmental authority is a party, **increases** the existing quantitative threshold for such

22 The adopting release is available here.

23 For more information, *see* our prior alert "SEC Adopts Amendments to Modernize Disclosures and Adds Human Capital Resources as a Disclosure Topic: Key Action Items and Considerations for US Public Companies."

environmental proceedings disclosure from $100,000 to **$300,000**. However, the amended rule also allows a company to opt for a different threshold of the lesser of $1 million or one percent of the current assets of the registrant and its subsidiaries on a consolidated basis, if the company:

- determines such alternative threshold is "reasonably designed to result in disclosure of any such proceeding that is material to the business or financial condition"; and
- discloses the threshold "in each annual and quarterly report," including any change thereto.

Given the hybrid threshold for disclosing environmental proceedings with governmental authorities, companies facing environmental proceedings should consider the nature and anticipated short- and long-term impacts of past and current environmental proceedings and determine the appropriate monetary threshold for their company under the amended rule.

In the end, companies will need to weigh the appropriateness and desire for a threshold higher than $300,000 against the requirement to publicly disclose, in each annual and quarterly report, their materiality threshold for disclosing such proceedings.

- *Hyperlinks and Cross-References for Legal Proceedings Disclosure Specifically Allowed*. In light of the November 9, 2020 rule amendments, companies should consider providing their Legal Proceedings section disclosure in response to Item 103 of Regulation S-K by including a hyperlink or cross-reference to legal proceedings disclosure elsewhere in the same document, such as MD&A, Risk Factors or a note to the financial statements. Many companies already provide a cross-reference, and should also consider providing a hyperlink for ease of navigability in their Form 10-K.[24]

(4) **COVID-19 Disclosure**. Now that we are almost one year into the COVID-19 pandemic, disclosure regarding the impact of the pandemic on your company should be more concrete and provide investors with clearer information on the impact to date, rather than only providing information about the uncertainties regarding the impact of the pandemic on the company.[25]

The key impacts of the pandemic on your company should be identified, assessed and described; these impacts may include, but are not limited to information on liquidity, operational adjustments, health and safety of employees, any material changes in the company's debt, loans and credit, any material changes to equity investments, impairment of assets, rent concessions and government assistance related to COVID-19.

In addition to giving rise to SEC comment letters, COVID-19 disclosures have recently led to several shareholder derivative suits[26] and at least one high-profile SEC administrative action against a corporate issuer under Section 13(a) of the Exchange Act alleging, in each case, misleading or omitted statements.[27] In particular, in the enforcement action, the SEC found that the company's filings were misleading when the company disclosed that it was "operating sustainably", while the company's own internal documents at the time showed that the company was losing significant cash each week and that

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24 Item 103 requires disclosure of any material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the company or any of its subsidiaries is a party, and similar proceedings known to be contemplated by governmental authorities. Companies hyperlinking or cross-referencing another disclosure should ensure that separate disclosure meets Item 103's particular disclosure requirements (*i.e.*, the name of the court/agency in which the proceedings are pending, the date instituted, the principal parties and a description of the factual basis alleged to underlie the proceeding and the relief sought).

25 For more information, *see* our prior alerts, " COVID-19 Legal Issues and Considerations", "SEC Takes Additional Actions Helping Public Companies Address Impact of COVID-19", "Practical Tips for Preparing Upcoming Quarterly Disclosures" and "SEC Emphasizes Importance of Robust Forward-Looking Disclosure for Q1 to Address COVID-19."

26 According to the Stanford Law School Securities Class Action Clearinghouse, available here, as of January 20, 2021, 21 securities class action lawsuits had been filed by shareholders accusing companies of failing to disclose or downplaying the risks related to the COVID-19 pandemic, failing to disclose or misrepresenting the extent to which it has affected the company's operations or financial results, or making false statements about or products related to COVID-19.

27 *See* the SEC's order against The Cheesecake Factory, available here.

the company only had four months of cash remaining.[28] In commenting on the action, former SEC Chairman Jay Clayton noted that "it is important that issuers continue their proactive, principles-based approach to disclosure, tailoring these disclosures to the firm and industry-specific effects of the pandemic on their business and operations".

(5) Pay Attention to Non-GAAP Compliance. Companies should also carefully review non-GAAP adjustments relating to the COVID-19 pandemic to ensure compliance with applicable SEC rules. The SEC continues to focus on non-GAAP measures, so it is important to pay careful attention to the use and disclosure of such measures each fiscal quarter. Recent SEC guidance has emphasized the following:

- Ensure that when a non-GAAP measure is used, the comparable GAAP measure is disclosed with equal or greater prominence, and a reconciliation of the two measures provided.
- Maintain consistent treatment of items between periods, or otherwise provide adequate disclosure about the reason for any change in treatment. For example, if there is a COVID-19 adjustment for an item during the current reporting period, and that adjustment was not made during the prior period, the company should provide sufficient disclosure regarding the change, including (i) the differences in the way the metric is calculated, (ii) the reasons for such changes, and (iii) the effects of any such change on the amounts or other information being disclosed.[29]
- To the extent a company presents a non-GAAP financial measure or performance metric to adjust for or explain the impact of COVID-19, it should highlight why management finds the measure or metric useful and how it helps investors assess the impact of COVID-19 on the company's financial position and results of operations.

Moreover, the Staff has reminded companies that it is not appropriate for a company to present non-GAAP financial measures or metrics for the sole purpose of presenting a more favorable view of the company. Rather, the Staff believes the acceptable purpose of non-GAAP measures is to share with investors "how management and the Board are analyzing the current and potential impact of COVID-19 on the company's financial condition and operating results."

(6) Key Performance Indicators ("KPIs"): Include in MD&A and Comply with SEC Guidance. In accordance with recent SEC guidance, companies should keep in mind that KPIs should be included in MD&A, as MD&A should provide a snapshot of a company's performance through the eyes of management. This may necessitate disclosure of material financial and non-financial metrics—KPIs—used by management to manage or evaluate the performance of the business.

In addition, companies should consider what additional information may be necessary to provide adequate context for an investor to understand the KPI metric presented. In this regard, the SEC generally expects the following disclosures to accompany any KPI metric:[30]

- a clear definition of the metric and how it is calculated,
- a statement indicating the reasons why the metric provides useful information to investors, and
- a statement indicating how management uses the metric in managing or monitoring the performance of the business.

(7) Critical Audit Matters ("CAMs").[31] For the first time this year, accelerated filers and non-accelerated filers will be subject to CAM requirements, which are applicable to such filers for fiscal years ending on or

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28 *See* the SEC's press release, available here.

29 For more information, *see* our prior alert, "SEC Releases New Guidance on KPIs."

30 For more information, *see* our prior alert, "SEC Releases New Guidance on KPIs."

31 For more information, *see* our prior alert, "SEC Approves PCAOB's New Audit Report Standard to Enhance the Relevance of the Auditor's Report to Investors and Other Market Participants." Also *see* AS 3101, available here.

after December 15, 2020. Last year, large accelerated filers disclosed CAMs for the first time. Emerging growth companies are exempt from CAM disclosure requirements.

A CAM is any matter arising from the audit of the financial statements that was communicated or required to be communicated to the audit committee and that: (i) relates to accounts or disclosures that are material to the financial statements and (ii) involved especially challenging, subjective or complex auditor judgment. For any CAM, the auditor must disclose the principal considerations that led the auditor to determine that the matter is a CAM and how the CAM was addressed in the audit, among other items.

According to a recent report issued by the PCAOB, the most frequently communicated CAMs have related to revenue recognition, goodwill, other intangible assets, and business combinations.[32] It is important for a company to engage with its auditor on a regular basis regarding potential CAM disclosure, and to ensure that disclosure is consistent throughout an annual report with respect to any matter disclosed as a CAM.[33]

(8) **Risk Factors: What to Include**: For upcoming Form 10-Ks, a number of recent trends and events may impact risk factor disclosures, as well as disclosures in other sections of the report. Although each company will need to assess its own material risks and tailor risk factors to its unique circumstances, below is a list highlighting certain areas of SEC focus and key trends that a company should consider when assessing its risk factors.

Companies should be mindful of providing thoughtful, accurate and thorough risk factor disclosure, as recent SEC enforcement actions indicate the SEC is focused on misrepresentations or omissions in connection with risk factors. In particular, in recent SEC enforcement actions, the SEC has alleged that statements in a company's risk factors were materially misleading because a company stated that an event only "may" or "could" occur, but the event was no longer hypothetical at the time of the disclosure.[11] Accordingly, risk factor disclosure should clarify whether a potential material risk has in fact occurred to some degree (whether or not the degree of occurrence is material on its own).

- ***COVID-19:*** Companies should ensure their risk factor disclosure related to COVID-19 is appropriately robust and specific. It is important to focus the discussion on the actual, specific risks the company faces, as the SEC has repeatedly commented on risk factor disclosures that only touch on general economic or societal impacts of COVID-19 and do not go far enough in describing company-specific COVID-19-related risks. A company should ensure that its risk factors accurately and fully describe the risks it faces, including risks that have already had an impact on the company, rather than describing these risks as merely hypothetical.[34] For example, one recent SEC comment

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32 Available here.

33 Large accelerated filers were already subject to the CAM requirements, and for any CAM, the auditor must disclose the principal considerations that led the auditor to determine that the matter is a CAM and how the CAM was addressed in the audit, among other items. A CAM is any matter arising from the audit of the financial statements that was communicated or required to be communicated to the audit committee and that: (i) relates to accounts or disclosures that are material to the financial statements and (ii) involved especially challenging, subjective or complex auditor judgment. The PCAOB's standard also provides a non-exclusive list of factors to be considered by an auditor to determine whether a matter is a CAM, including risks of material misstatement, the extent of audit effort and subjectivity required, and the degree of judgment involving estimates with significant measurement uncertainty.

It is important for a company to engage with its auditor early and on a regular basis regarding potential CAM disclosure. The PCAOB noted that some audit teams began the process to determine CAMs as early as the second or third quarter of the fiscal year and that starting early provided ample time to identify CAMs and draft disclosure. For companies reporting CAMs in their upcoming Form 10-Ks, it will be important to ensure that disclosure is consistent throughout an annual report with respect to any matter disclosed as a CAM.

34 For example, in September 2019, a major pharmaceutical company agreed to pay a $30 million penalty to the SEC for using hypothetical language. After a government agency informed the company that it had misclassified its most profitable product as a generic drug, the company's risk factor disclosures in its annual reports continued to state that a government entity "may" take a position that is contrary to that classification. The SEC concluded that using the term "may" was materially misleading because the company knew at the time that a government agency had in fact taken a contrary position. For more information, *see* "Press Release 2019-194, Mylan to Pay $30 Million for Disclosure and Accounting Failure Relating to EpiPen" (Sept. 27, 2019), *available* here.

asked a company to expand its risk factor discussion, which merely discussed a general decrease in consumer spending momentum, to describe "the reasonably likely known effects of the coronavirus on [its] business" and, to address, to the extent material, "the expected impact on [its] results of operation and financial condition for fiscal 2020."

Furthermore, COVID-19 is no longer a novel consideration from a disclosure perspective, and while the landscape continues to shift, and it is therefore important for companies to discuss company-specific risks to the extent possible, rather than merely disclosing that the risks related to the pandemic remain uncertain. Companies should also carefully consider whether any significant trend or uncertainty that management is closely monitoring and/or discussed with the board is appropriate for MD&A disclosure.

- ***Human Capital Resources***: In light of the recent rule changes requiring human capital management disclosure (discussed above), as well as heightened focus on this issue by investors, companies should assess what—if any—material issues their company faces with respect to human capital resources and consider any appropriate updates to risk factor disclosure. This could include risks related to the ability to attract and retain skilled employees, changes in laws or regulations regarding employees outside of the US, employee health and safety issues, increases in labor costs and increased employee turnover.

- ***Brexit***: When the UK withdrew from the EU ("Brexit") on January 31, 2020, it began a transition period in which to negotiate a new trading relationship for goods and services that ended on December 31, 2020. On December 24, 2020, the UK and EU announced they had entered into a post-Brexit deal on certain aspects of trade and other strategic and political issues. Given the newness of the deal, companies are likely still evaluating the potential risks and financial, trade, regulatory and legal implications of this new trade deal. However, it is important to keep investors informed about the nature and extent of known and potential risks and the steps companies are taking to address them. Through comment letters, guidance and speeches, the SEC has cautioned companies against boilerplate disclosure in this area, and if Brexit-related risks represent material risks to the company, disclosure should be tailored and should describe with sufficient specificity how Brexit is expected to impact the company and its operations. SEC Staff may closely review SEC filings to assess whether companies adequately address the impact of Brexit, including indirectly through other businesses and individuals on whom the company relies.[35]

- ***Cybersecurity***: As cybersecurity incidents and data misuse continue to proliferate, the SEC staff has been focusing on, and providing comments regarding, cybersecurity and privacy disclosures. As part of this focus, the SEC staff monitors press reports and may raise questions directly with affected companies about the sufficiency of cybersecurity or privacy disclosures in SEC reports on that basis. SEC guidance,[36] as well as high-profile enforcement actions for inadequate or misleading disclosures,[37] emphasizes that cybersecurity and complying with personal data rights pose economic, operational and reputational risks that can impact any company. With respect to disclosure issues, recent cases caution against framing risk factor disclosures in hypothetical terms without addressing actual incidents experienced by a company.[38]

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35 *See* "SEC Rulemaking Over the Past Year, the Road Ahead and Challenges Posed by Brexit, LIBOR Transition and Cybersecurity Risks" (December 6, 2018), available here; *see also* "Applying a Principles-Based Approach to Disclosing Complex, Uncertain and Evolving Risks" (March 15, 2019), available here.

36 In February 2018, the SEC published interpretive guidance to assist public companies in preparing disclosures about cybersecurity risks and incidents, available here.

37 With respect to cybersecurity, the SEC found that Yahoo's risk factor disclosures in its annual and quarterly reports were materially misleading in that they claimed the company only faced the "risk of potential future data breaches" that might expose the company to loss and liability "without disclosing that a massive data breach had in fact already occurred." The SEC's action is available here. For more information, *see* our prior alert, "SEC Fines Yahoo $35 Million for Failure to Timely Disclose a Cyber Breach."

38 For example, the Yahoo case focused on disclosure of "possible" data breaches when the company had already experienced such a breach.

Material cybersecurity and data privacy risks must be disclosed and, to the extent the company has already experienced actual cybersecurity or data misuse incidents, such occurrences and their impact on the company must be described. In addition, other specific disclosure with respect to cyber and data risks associated with suppliers, acquisition targets and other third parties may be warranted.

Meanwhile, the impact on corporate operations of an ever-expanding and complex array of personal data privacy laws throughout the world often requires additional risk disclosures. Most notable in this regard is compliance with the European Union's General Data Protection Regulation (the "GDPR"), which became effective in 2018 and remains a material issue for many companies regardless of whether they have a physical presence in Europe. Compliance with the GDPR can require changes to a company's business practices on whether and how to collect and use certain types of personal data, affect a company's ability to transfer personal data internationally, impact decisions to expand into certain regions or lines of business, and subject companies to sizable financial penalties, all of which could materially adversely affect profitability and outlook. Similarly, in light of the California Consumer Privacy Act (the "CCPA"), which became effective on January 1, 2020, companies should identify and disclose any material risks of this law to their business model, especially with respect to restrictions on the broadly defined "sale" of personal data. Companies should consider what non-boilerplate disclosures, if any, are necessary, as well as the business impact of compliance, with these and other emerging data privacy laws and regulations.

- ***IP and Technology Risks***: In December 2019, the SEC Staff released guidance specifically calling on companies to assess risks related to the potential theft or compromise of their technology, data or intellectual property in connection with their international operations and disclose them where material.[39] Beyond direct intrusions, the guidance notes that companies may also face theft or compromise of these assets via indirect routes. For example, a company's products may be reverse engineered by joint venture parties, including those affiliated with state actors. The guidance encourages companies to consider a range of questions when assessing these risks, including whether they are operating in foreign jurisdictions where the ability to enforce rights over intellectual property is limited as a statutory or practical matter, and whether they have controls and procedures in place to adequately protect technology and intellectual property. The Staff also emphasized that disclosure of material risks should be specifically tailored, and that where a company's technology, data or intellectual property is being (or previously was) materially compromised, hypothetical disclosure of potential risks is not sufficient to satisfy a company's reporting obligations. Furthermore, companies should continue to consider this evolving area of risk and evaluate its materiality on an ongoing basis.

- ***LIBOR***: In light of the expected discontinuation of LIBOR after 2021,[40] the SEC staff issued guidance in July 2019 [41] stating that: (i) companies should consider disclosing their efforts to date to identify and mitigate associated risks and assess their impacts, as well as disclosing any significant matters yet to be addressed; (ii) if a material exposure to LIBOR has been identified but the company cannot yet reasonably estimate the expected impact, companies should consider disclosing that fact; and (iii) disclosures that allow investors to see this issue through the eyes of management are likely to be the most useful for investors (such as information used by management and the board in assessing and monitoring how transitioning from LIBOR may impact the company). The SEC staff expressly indicated that it is actively monitoring the extent to which risks related to the discontinuation of LIBOR are being addressed, and noted that companies should assess whether disclosure may be appropriate in their risk factor section as well as in the MD&A, the business section, the financial statements and/or the discussion of board risk oversight responsibilities.

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39 The guidance is available here.

40 LIBOR is an indicative measure of the average interest rate at which major global banks could borrow from one another and is quoted for multiple currencies and time frames. It is used extensively in the US and globally as a "benchmark" or "reference rate" for various commercial and financial contracts. *See* SEC guidance available here.

41 Available here.

- ***Regulatory***: Changes and potential changes in law, regulation, policy and/or political leadership, including the new regulatory agenda of the Biden administration, may necessitate modifications to risk factor disclosure for certain companies. Some examples include: current and potential changes to immigration policies, minimum wage, tariffs, taxes, environmental policies, health care and other political developments in the US.

- ***Environmental***: Environmental issues such as climate change have been receiving increased attention, and companies should consider whether they present material risks for their businesses. Risk factor disclosure related to environmental issues should be tailored to the specific circumstances of a company and can address a number of topics, including applicable environmental regulations and the impact of climate change on a company's business, such as risks of increased costs or reduced demand for products, carbon asset risk, risks due to severe weather events, such as forest fires on the west coast, and management of greenhouse gas emissions, among other environmental issues. Environmental risk factors should also address risks to companies from anticipated changes to regulations affecting their businesses. The incoming Biden administration supports implementing laws and policies that will take a more aggressive approach towards regulating impacts to the environment. Notably, President Biden is expected to prioritize the domestic and international response to climate change. Climate change is reported to be one of four top-tier priorities for the new administration and on the day of his inauguration, President Biden took action through the signing of executive orders for the United States to rejoin the Paris Agreement, revoke a permit for the Keystone XL oil pipeline and review certain Trump administration environmental regulatory actions.

(9) Last but not Least, Consider Timing for Implementation of SEC's Latest Rule Amendments (Optional Beginning February 10, 2021; Mandatory for Fiscal Years Ending on or after August 9, 2021): Recent rule amendments effective February 10, 2021, made comprehensive changes to Item 301, Item 302 and Item 303 of Regulation S-K. However, these changes will only be mandatory for Form 10-Ks filed for fiscal years ending on or after August 9, 2021. Prior to August 9, 2021, the rule amendments may be voluntarily complied with on an item by item basis (*i.e.,* with respect to all of the changes to each respective item of Regulation S-K that was amended).[42]

- ***Selected Financial Data Disclosure (Item 301)***. Item 301 of Regulation S-K generally requires companies to furnish selected financial data in comparative tabular form for each of the last five fiscal years and any additional fiscal years necessary to keep the information from being misleading.[43] Under the recent rule amendments, Form 10-Ks filed on or after February 10, 2021 may eliminate selected financial information disclosure required by Item 301 of Regulation S-K. However, in its adopting release, the SEC still encouraged registrants to "consider whether trend information for periods earlier than those presented in the financial statements may be necessary as part of MD&A's objective to 'provide material information relevant to an assessment of the financial condition and results of operations.'" In addition, the SEC noted that it encourages companies to consider whether a "tabular presentation of relevant financial or other information, as part of an introductory section or overview…may help a reader's understanding of MD&A."[44]

- ***Selected Quarterly Financial Data (Item 302)***. Item 302(a) of Regulation S-K requires disclosure of selected quarterly financial data of specified operational results and variances in these results from amounts previously reported on a Form 10-Q.[45] Under the recent rule amendments, the SEC decided to retain Item 302 and streamline its requirements to require disclosure "only when there are one or more retrospective changes that pertain to the statements of comprehensive income for any of the quarters within the two most recent fiscal years and any subsequent interim period for which financial statements are included or required to be included…and that, individually or in the aggregate, are

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42 For a table summarizing the amendments, please *see* page 8 of the adopting release, available here.

43 Smaller reporting companies are not required to provide Item 301 information and EGCs need not present selected financial data for any period prior to the earliest audited financial statements presented.

44 *See* adopting release here.

45 Item 302(a) does not apply to SRCs, FPIs, first-time registrants conducting an IPO and registrants that are only required to file reports pursuant to Section 15(d) of the Exchange Act.

material." The amendments further require registrants to: (i) provide an explanation of the reasons for any such material retrospective changes and (ii) disclose, for each affected quarterly period and the fourth quarter in the affected year, summarized financial information related to the statements of comprehensive income and earnings per share reflecting such changes. Accordingly, once a company opts to implement these rule changes, it will need to carefully assess whether any such disclosure will be required. As examples of the type of "retrospective change" that may trigger Item 302(a) disclosure, the SEC noted the following: a correction of an error, the disposition of a business that is accounted for as discontinued operations, a reorganization of entities under common control, or a change in an accounting principle. The SEC cautioned, however, that these examples are not intended to be an exhaustive list and may not always be material such that disclosure would be required under amended Item 302(a).

- ***Streamlined MD&A (Item 303)*:** As part of the recent rule amendments, the SEC also made substantial changes to MD&A requirements under Item 303 of Regulation S-K, which changes will require an assessment of a company's current MD&A disclosure and the required changes for a particular company's disclosure to align with the recent rule amendments. For upcoming Form 10-Ks filed in 2021 for calendar year-end companies, there is no requirement to implement these changes, but companies should keep certain changes in mind ahead of their mandatory implementation next year. These rule changes include:
  - Clarifying in amended Item 303(b) that where there are material changes in a line item of a company's financial statements, including where material changes within a line item offset one another, disclosure of the underlying reasons for these material changes in quantitative and qualitative terms is required; and
  - Eliminating the contractual obligations table in Item 303(a)(5), but amending the liquidity and capital resources disclosure requirements in Item 303(b)(1) to specifically require disclosure of material cash requirements from known contractual and other obligations, including specifying the type of obligation and the relevant time period for the related cash requirements.

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Appendix A

Sample Attestation

[Company Name]

ELECTRONIC SIGNATURE ATTESTATION FOR SEC FILINGS

For purposes of authenticating my typed signature on filings made by [Company Name] (the "Company") with the Securities and Exchange Commission through its Electronic Data Gathering, Analysis, and Retrieval system (EDGAR) (each such authentication, an "Authentication Document"), I hereby attest that my electronic signature on any Authentication Document constitutes the legal equivalent of my manual signature.

I understand that I may revoke this attestation by delivering a revocation to the Company in writing. I understand that this attestation is effective when signed and delivered to the Company.

Signature:
Name:
Date:

[Company Use Only:]
Date Received:

To be retained by the Company for so long as signatory uses an electronic signature to sign Authentication Documents, and for a minimum period of seven years following the date of the most recent electronically signed Authentication Document.